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Why should investors stay positive on the Asian real estate markets?

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Almost as certain as night following day, the booming regional property market has followed the slump in the financial markets. Buyers, previously enriched by their gains in the stock market, are staying away. Property investors, many of them speculators, basically, are no longer chasing up prices for a quick flip. Many of them are stuck with loans that they struggle to pay - a situation made much worse with property devaluation. Many property developers have also been saddled with projects with no takers, while servicing mounting interest costs. Building contractors, who rely heavily on the property market for business, are also affected. What is the outlook and when will the regional property market recover? Should one stay away from the Asian real estate market?

For Justin Chiu, crises present investors with opportunities. "There is no denying that the current outlook for Asian economies and real estate market is cloudy. Uncertainties remain as to when the global financial crisis will abate," said Chiu, executive director of Cheung Kong Holdings, a Hong Kong-based property development and investment company chaired by Li Ka-Shing, Asia's richest man and arguably, most renowned entrepreneur.

Singapore private property prices, for example, had dropped 20% from its recent peak reached during the second quarter last year. This was after a heady 31% gain between 2007 and 2008, fuelled by a roaring stock market and (some say misguided) optimism over Singapore's prospects as a global hub for the wealthy to live, work and play. Across the region, property prices across various sectors – residential, industrial, commercial, office, have all weakened significantly.

While Chiu might not be speaking as the most neutral party on the property market, he nevertheless brings with him nearly three decades of regional experience in this field. Chiu is also the chairman of ARA Asset Management Limited, the manager of various property investment funds, companies, as well as four real estate investment trusts (reits), including two publicly-traded in Singapore: Suntec reit and Fortune reit.

"While the crisis works its way out, opportunities are abundant for both retail and institutional real estate investors who are willing to look beyond the cyclical nature inherent to real estate markets" said Chiu. He was speaking at the graduation ceremony of the advanced management programme, jointly organised by the Building and Construction Authority and Singapore Management University's office of executive education. The 18-day programme is aimed at developing the management capability of companies in the building and construction industry, including contractors, engineering services providers, architectural firms and property developers.

Stronger fundamentals

Compared to the Asian financial crisis that happened just over a decade ago, when widespread social unrest happened and where even governments were brought down, Chiu sees Asian economies of today, "galvanised" by the crisis, as a different animal. "Asia is now stronger. Tough but necessary reforms were implemented, which has enabled Asia, on a strong footing, to withstand financial and economic headwinds, and to ensure swift recovery once the dust settles," he said, referring to sound measures like greater fiscal and monetary discipline across all levels. Compared to the pre-crisis years, Asian economies now have lower foreign debts and higher foreign reserves. Excessive investments were curbed and banks, better capitalised.

Furthermore, Asian economies are undergoing a "dynamic change" in their demographics. In many countries, the younger populace is a growing proportion. They add to the ranks of a middle class that is eager to spend and boost their quality of lives. Almost certainly, they will be looking for a bigger, better and nicer roof over their heads that they can call their own, said Chiu.

Investors should approach the Asian markets with a new attitude. "In the past, the rationale for investing in Asia was to ride on Asia's strong economic growth. However, as the global financial environment has changed dramatically, the challenge now is to identify and to invest in the best deal among the myriad of noisy and active markets," said Chiu.

China is a market on Cheung Kong's radar. "China, with its strong fundamentals, sizeable economy and changing demographics, is proving to be an irresistible choice for all investors," said Chiu. But needless to say, the global economic slowdown has hit China hard as well. Many factories have ground to a halt or shut down completely. Orders have vaporised. Steep declines in exports form a stark contrast to the blistering growth of the previous years. Yet, China is holding its chin high, tapping on its foreign reserves for a huge stimulus package aimed at maintaining a GDP growth rate of 8% over the next few years.

"As the trend of economic expansion and urbanisation continues in China, it will result in rising income, and along with it, demand for better quality housing and more sophisticated retail properties," Chiu noted. The growth will not be limited to the residential sectors. "As the Chinese economy moves slowly from production-oriented to service-oriented, the demand for good commercial space, that is retail mall and office space, will grow. This will have a positive impact on the value of our commercial properties," he said.

Public spending

There is another reason why Chiu is optimistic. While the private sector is cutting back on spending and investment, governments in many countries are doing the exact opposite, investing heavily to pick up the slack. In a typical case of pump-priming, many Asian governments have earmarked spending on new major infrastructural projects or brought forward those in the pipeline. Such activities will "add fuel" to the growth of the economy, said Chiu.

From his point of view, such domestic spending will help Asia reduce its heavy reliance on export-driven growth, and instead, focus more on their domestic, less volatile markets. "Asian governments have implemented and are continuing to implement measures and policies that encourage consumption, job creation and home ownership," he noted.

Singapore is one of the Asian countries spending heavily on infrastructure projects. Last year, the government awarded contracts worth $34.6 billion - a record high. Several projects were brought forward to maintain a steady pipeline for the local construction sector.

However, not all local contractors believe that they will stand to gain substantially from these government contracts, which often involve big-ticket and technically challenging projects, requiring high levels of specialisation. For example, a major chunk of the Singapore government spending goes into building new transport systems like the MRT lines. Such projects require such elaborate tunnelling works that only big multinational foreign contractors can bid and win. Local contractors, in contrast, are often left to fight over smaller projects.

"The way to get around is to form long term joint ventures with the foreign contractors, and over the years, some transfer of technology takes place. Perhaps, you can then stand on your own feet in the future to compete successfully," said Bonaventure Lek, Singapore deputy general manager of Shimizu Corporation, one of the top five Japanese contractors, speaking at the same event.

"Even though the main contract may go to foreign contractors, by and large, it is the practice of the industry to subcontract out all the work anyway. And who are the subcontractors?" asked Lek, as he pointed out that nearly all subcontractors are local companies. "So, ultimately, it will still benefit the whole industry."

Correct pricing

A recovery in the property market will depend largely on whether there are buyers willing to bite. Chiu is optimistic, especially for Hong Kong and Singapore markets. "Their (buyers) pockets are still deep. I don't really see any major problems in these two markets, except that as a developer, you've got to be realistic," he said.

What matters, is the developers' willingness to put behind the euphoria during the recent boom and price their projects at a level that is agreeable with the buyers. Gone, at least for now, are the days when buyers will trip over one another to hand in their down payment during new property launches, never mind the price.

"You've got to be very realistic in your pricing. But of course, if you have the holding power and you can wait, the market is going to come back and you don't really need to fire sale. But if you really want to sell, you've got to be realistic and sell at market prices," said Chiu.

Just recently, Cheung Kong launched a new residential project at New Territories, Hong Kong. "We priced it to the market, we sold more than 1,000 units overnight and we reaped about HKD$2 billion. It shows that people are still confident and they still have the money, but they also know how to hunt for the best deal. So as long as you price it right, everything sells," said Chiu.

Referring to the Singapore market, especially the so-called "mass" or lower-end segment, Chiu thinks that as long as developers are not too "aggressive" in their pricing, the sale will go well. But in the same vein, he also reminds developers not to be in a hurry to let go, especially if they can handle their cash-flow. "As a developer, if I don't need to fire sale; if I can hold for one, two years, then hold. I am quite sure the market will come back," he said.

Recent Asian economic history backs Chiu up. The last few economic cycles have averaged between five to seven years, implying a peak-to-trough period of around three years. The US-led financial crisis started back in the second half of 2007, with the real economy's downturn following soon after. "I would say, towards the end of this year, we will be on the road to recovery. We can start to look around and hunt for the best deal," said Chiu. "The challenge for us is not whether Asia will recover or not; the challenge for us is to identify the best deal available."

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